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SENSITIVE
SIPDIS

DEPARTMENT FOR EEB/ESC/IEC

E.O. 12958: N/A

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SUBJECT: CHINA SEEKS INVESTMENT IN STRATEGIC RARE EARTHS

¶1. (SBU) SUMMARY: State-owned company China Non-Ferrous Metal Mining Corporation is seeking to buy a controlling stake in Australian rare earth company Lynas, which manages one of only two globally significant projects outside of China. The Foreign Investment Review Board extended its review of the proposal, given that China already controls 97% of global rare earths supply. END SUMMARY.

INVESTMENT PROPOSAL BY CHINA NON-FERROUS MINING

¶2. (SBU) China Non-Ferrous Metal Mining (CNMC), a state-owned company, is proposing to spend A\$500 million for a majority stake in the Australian rare earth company Lynas, which operates one of only a few globally significant advanced projects outside of China (others are in California, the CIS and Brazil). Its Mount Weld rare earth project is one of Western Australia's biggest new mining developments and includes a processing plant in Malaysia.

¶3. (SBU) Lynas was positioning itself as an alternative supplier to Chinese companies before the global financial crisis. But financing difficulties forced the company to turn to foreign investors for funding in order to complete construction of the Mount Weld project. CNMC plans to invest an initial A\$252 million to bring the mine into production by 2010. The financing plan involves Chinese banks and would give CNMC a 51.6% stake in Lynas. Lynas' existing 5-year contracts cover 75% of its first-stage output and 25% of its second-stage output with customers in the US, Europe and Japan. A change in ownership, however, could affect the direction of future sales.

STRATEGIC SIGNIFICANCE OF THE PROPOSAL

¶4. (SBU) About 97% of global production of a collection of elements called rare earths -- essential ingredients in advanced weaponry, fighter jets and radar equipment -- takes place in China. Chinese control of the global supply of rare earths means that the Chinese government could influence access to supply. Concerns in the U.S. over security for the supply of these minerals prompted the filing of a WTO case against China in June 2009 for imposing export quotas on rare earths, as well as a bill currently before Congress, which would require a report, to be completed by next year, on the strategic significance of the minerals for the U.S.

FOREIGN INVESTMENT REVIEW BOARD REQUESTS DELAY

¶5. (U) In early July 2009 Australia's Foreign Investment Review Board (FIRB) asked CNMC to withdraw and resubmit its application, starting a new 30-day review process. If approved by the FIRB, Lynas would convene a shareholder meeting in September 2009 to approve the CNMC transaction. In the local press, academic and

mining industry experts have warned recently about the danger of facilitating even more control over rare earths to China.

¶6. (SBU) COMMENT: Earlier this year the FIRB allowed another Chinese company to buy a 25% stake in a less advanced rare earths explorer, Arafura Resources. Yet Treasurer Swan blocked a China Minmetals-proposed acquisition of Australian OZ Minerals' Prominent Hill mine on national security grounds, making the likelihood of approval of CNMC's proposal by the FIRB uncertain. The possibility of increased tensions between China and Australia over the detention of a Rio Tinto executive in Shanghai could add to the uncertainty. If approval by the FIRB is given, significant conditions are likely. If approval by the FIRB is given, significant conditions are likely to be imposed given the strategic interests at stake. END COMMENT.

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